

Samuelson Says Nothing About Trade Policy

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Protectionism has long enjoyed populist appeal, but has not achieved intellectual respectability. Quite simply, it lacked a leading economist guru to champion its cause. Therefore protectionists the world over must be jumping for joy at having found an illustrious one, namely Paul Samuelson. Gurus and champions don't come any bigger than that.

But what has Professor Samuelson actually proved in his recent article, "Where Ricardo and Mill Rebut and Confirm Arguments of Mainstream Economist Supporting Globalization" (Summer, 2004, pp. 135-146)? He compared two situations: [1] The U.S. has a free trade policy, and China has low productivity in the sectors where the US is an exporter. [2] The US has a free trade policy, and China has high productivity in these same sectors. The U.S. terms of trade are worse, and the aggregate US economic welfare is lower, in [2] than in [1]. (Professor Samuelson focuses on a special numerical example where the Chinese productivity rises exactly to the point where U.S. exports are reduced to zero, but that is irrelevant for the argument. It is just a kind of worst-case scenario.)

Have U.S. terms of trade deteriorated in recent years? From the beginning of 1990 through the end of 2003, the BLS index of import prices rose by 5.4 percent, while export prices rose by 5.9 percent. If we exclude petroleum products (presumably not the point of Professor Samuelson's arguments) import prices rose by only 1.7 percent. Thus, U.S. terms of trade have been steady, or perhaps even improving, since 1990.

Even if ignore the empirical counterevidence, Professor Samuelson's theoretical proposition remains valid as a logical possibility. But what are its policy implications? Alas, none. Neither trade policy, nor any other available policy, will take us back to the desirable situation [1]. The only action that can restore [1] is to "bomb China back into the stone age" of their older lower productivity. We sincerely hope Professor Samuelson is not proposing that. The only practical policy question facing the United States now is: given that we are now in situation [2], do we go on trading freely or not? Should we switch to the protectionist alternative [3], namely Fortress America? If our objective is to maximize aggregate U.S. economic welfare, the answer is unequivocally no. All the standard arguments apply to this comparison, and say that [2] is better for aggregate U.S. economic welfare than [3]. Only in Professor Samuelson's worst-case scenario is there no difference between [2] and [3], because if even with a free trade policy the comparative advantage configuration is such that our trade is exactly zero, then there is no gain from trade. However, there is no loss from keeping our trade free either, so [2] and [3] are equivalent in that case. In all other cases, [2] is positively superior to [3] from the aggregate U.S. perspective. Therefore protectionists should take no comfort from Professor Samuelson's intervention on their behalf; they must still go on looking for their guru.

Of course aggregate economic gains are not enough to establish either the ethical desirability or political practicality of the policy of free trade on its own, unless mechanisms whereby winners actually compensate losers are in place. Therefore the analysis recommends a policy package – keep trade free, but compensate the losers it creates. We believe that Professor Samuelson and we are in agreement on this.